

Report on the International Economy

June 2019



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Abbreviations

CPI	consumer price index
ČNB	Česká národní banka
EA	euro area
ECB	European Central Bank
EC	European Commission
EMEs	emerging market economies
EONIA	euro overnight index average
ESA 2010	European System of Accounts 2010
ESI	Economic Sentiment Indicator (European Commission)
EU	European Union
EUR	euro
EURIBOR	euro interbank offered rate
Eurostat	statistical office of the European Union
FDI	foreign direct investment
GDP	gross domestic product
GNDI	gross national disposable income
GNI	gross national income
HICP	Harmonised Index of Consumer Prices
IMF	International Monetary Fund
MFI	monetary financial institutions
MF SR	Ministry of Finance of the Slovak Republic
MMF	money market fund
MNB	Magyar Nemzeti Bank
MTF	NBS's Medium-Term Forecast (published on a quarterly basis)
NACE	Statistical Classification of Economic Activities in the European Community (Rev. 2)
NARKS	National Association of Real Estate Offices of Slovakia
NBP	Narodowy Bank Polski
NBS	Národná banka Slovenska
NEER	nominal effective exchange rate
NFC	non-financial corporation
NPISHs	non-profit institutions serving households
OECD	Organisation for Economic Co-operation and Development
p.a.	per annum
p.p.	percentage point
PMI	Purchasing Managers' Index
REER	real effective exchange rate
SASS	Slovenská asociácia správcovských spoločností – Slovak Association of Asset Management Companies

SME	small and medium-sized enterprise
SO SR	Statistical Office of the Slovak Republic
ULC	unit labour costs
ÚPSVR	Ústredie práce, sociálnych vecí a rodiny – Central Office of Labour, Social Affairs and Family
ÚRSO	Úrad pre reguláciu sieťových odvetví – Regulatory Office for Network Industries
USD	US dollar
VAT	value-added tax

Symbols used in the tables

- . - Data are not yet available.
- - Data do not exist / data are not applicable.
- (p) - Preliminary data

1 The global economy

The softening of global growth momentum observed in the second half of 2018 continued in the first quarter of 2019. The global GDP growth path was in synchronicity with world trade growth, which decelerated against a backdrop of lower manufacturing activity, rising trade tensions and a cooling of the technology cycle in Asia. In an environment of elevated uncertainty, investment growth moderated and there were declines in business and consumer confidence. Financial conditions in many countries reflected the impact of further monetary policy accommodation, or rather the pausing of anticipated monetary policy normalisation. More recently, however, the introduction of new tariffs has led to a tightening of financial conditions. Favourable labour market conditions in large economies have continued to support household income and household consumption expenditure. Some countries, in particular China, have loosened fiscal policy significantly, but fiscal stimulus in most countries remains limited.

The performance of advanced economies in the first quarter of 2019 surprised on the upside, though in several cases the improvement stemmed from one-off factors. In the United States, the positive impact of net exports and restocking on GDP growth was cancelled out by softening of domestic demand as a result of the partial federal government shutdown. The United Kingdom's economic growth was higher than expected in the first quarter, thanks to strong figures for investment and government expenditure. Inventories increased sharply, due to significant stock-building by businesses in the run-up to the original deadline for the UK's withdrawal from the European Union (Brexit);¹ however, the impact of this rise was offset by the strongest increase in imports since 2006. Japan's GDP growth was also stronger in the first quarter of 2019 than in the previous quarter, but with both private and public consumption decreasing and with investment growth decelerating, its acceleration was based entirely on imports falling more sharply than exports. This import slump, implying weak domestic demand, together with weakening foreign demand resulted in increasing debate about the consumption tax increase that is planned for October of this year. Euro area economic growth also increased in the first quarter, as private consumption continued to firm and investment growth remained solid. Net exports also made a positive contribution to GDP growth.

Despite its trade war with the United States, China did not report any signs of economic slowdown in the first months of 2019. Although China's foreign trade was affected by the trade conflict, as well as by more subdued

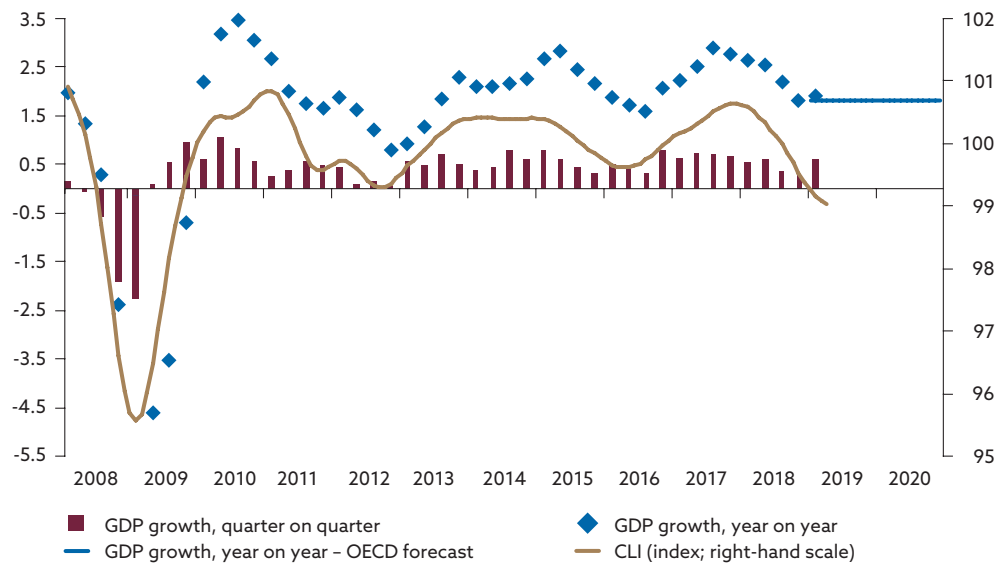
¹ Originally set for 29 March 2019, the deadline was postponed in April until 31 October 2019.

foreign demand, its annual GDP growth was the same in the first quarter as in the last quarter of 2018. Given retail sales developments, low inflationary pressures, and a solid increase in disposable income, the first-quarter growth is expected to have been driven by private consumption. Domestic demand was also buoyed by the fiscal stimulus impact on fixed capital investment. In India, too, economic growth in the first quarter was attributable to private consumption and investment, albeit to a lesser extent than in the previous quarter. The country's annual GDP growth slowed and was lower than China's for the first time in almost two years; hence India lost its position as the fastest-growing large economy. Russia's economic growth in the first quarter was among the weakest rates since the recession of 2015-16. This slowdown was probably related to an increase in VAT, rising inflation, declining sentiment, and subdued export growth resulting from warm weather in Europe and oil output quotas. After two years of relatively favourable progress, Brazil's GDP fell in the first quarter of 2019, thus raising concerns about a potential recession in Latin America's largest economy. Iron ore supply disruptions were one of the factors behind that outturn. At the same time, economic activity was dampened by net exports, which fell in response to a less benign external environment. The Brazilian economy was also affected by rising political tensions related to the new economic reform proposal, concerning mainly the pension system.

Reflecting favourable trends in advanced economies, economic activity growth across the OECD area accelerated to 0.6% in the first quarter of 2019, up from 0.3% in the fourth quarter of 2018. In year-on-year terms, too, GDP growth increased moderately, from 1.8% in the last three months of 2018 to 1.9% in the next three months. The Composite Leading Indicator for the OECD area² continued its downward trend in the first quarter and fell again in April 2019, thus implying a further slowdown of the global economy in the near term. Furthermore, the latest readings of the Global Composite Purchasing Managers' Index, whose average for April and May was below that for the first quarter, suggest that rising global trade tensions are being reflected in downward risks to the global GDP growth outlook. According to the IMF, the US-China trade dispute has so far had a relatively moderate impact on global growth, but its most recent escalation could more severely hurt business, dent financial market sentiment, disrupt global supply chains, and weigh on global growth.

² The CLIs for OECD countries are published on a monthly basis, and the most recent, published in June 2019, are for the period up to April 2019.

Chart 1
GDP growth and the CLI for the OECD area



Source: OECD.

Note: CLI - Composite Leading Indicator.

Global consumer price inflation slowed slightly in the first quarter of 2019; the average annual headline rate in the OECD area fell from 2.4% in December 2018 to 2.3% in March 2019. Contributing to the slowdown was a decrease in the energy component, which reflected movements in energy commodity prices. The core inflation rate was also slightly lower in March than in December, decreasing from 2.2% to 2.1%. There was, though, upward pressure on the headline rate from an increase in food inflation. In April, headline inflation rose to 2.5%, with the energy component having a strong upward impact - its acceleration driven by the pass-through of an upturn in prices of energy commodities, especially oil. Core inflation also contributed positively, as it edged up to 2.2%.

2 Commodities

The average commodity price index was lower in the first quarter of 2019 than in the last quarter of 2018. The decline in average energy commodities outweighed the impact of a slight increase in non-energy commodity prices.

Looking at energy commodity prices, the average price of a barrel of Brent crude oil maintained a rising trend throughout the first quarter of 2019 after bottoming out in December 2018; nevertheless, it did not exceed the average for the last quarter of 2018. The rising oil price was a response to the decision of OPEC and allied oil producers to trim output by 800,000 barrel per day from January. At the same time, the oil price was affected by reduced output in Iran and Venezuela following the imposition of US sanctions, by the optimism surrounding a trade deal reached between the United States and China, and an improvement in the outlook for Chinese manufacturing industry. The oil price continued increasing in April, when the US Administration announced it would be ending all waivers on its sanctions on imports of Iranian oil. Subsequently, however, the oil price broadly declined on the back of rising US oil output, expectations of an increase in OPEC output, and the escalating tensions between the United States and China.

The increase in average non-energy commodity prices in the first quarter was supported by metal prices and food commodity prices. The pick-up in metal prices was underpinned by improving financial market sentiment and by the anticipation of Chinese stimulus measures. Iron ore prices climbed following a mining accidents in Brazil and Australia, while zinc prices were boosted by a tightening of supply, after China, the world's largest zinc producer, imposed environmental protection measures on its zinc industry. Copper prices rose as stocks of the metal decreased. Aluminium prices had a dampening effect on the overall metal price index, as production outlooks were improved by the decision of the United States to lift sanctions on the Russian producer Rusal. As for food commodity prices in the first quarter, pork prices increased due to an outbreak of African swine fever in China and the consequent increase in pork demand from that country. On the other hand, decreases in wheat and coffee prices put downward pressure on the food commodity price index.

3 The United States

In the United States, economic growth in the first quarter of 2019 outperformed expectations. The annualised rate of GDP had been expected to moderate, owing to the partial federal government shutdown³ as well as to the gradual fading of fiscal stimulus effects, but in fact it accelerated to 3.1% (from 2.2% in the previous quarter). The year-on-year growth rate also increased, from 3.0% in the fourth quarter of 2018 to 3.2% in the first quarter of 2019.

Net exports accounted for around one-third of the GDP growth, as export growth increased and imports fell. Imports were starting to be significantly affected by the tariffs adopted in 2018. Changes in inventories also made a strongly positive contribution to GDP growth, an impact that ordinarily would be offset by that of foreign trade. The favourable effect of net exports and inventories cancelled out the impact of weaker domestic demand, which was a consequence of the partial federal government shutdown's downward impact on growth in private consumption and in fixed investment (owing mainly to lower investment in equipment). Thanks to investment in roads and transport infrastructure, the government sector contributed positively to economic growth.

US GDP growth for the whole of 2019 is expected to be lower year on year, due to the fading of the one-off factors that underpinned the first quarter's robust growth as well as to the fading of the positive fiscal stimulus effects together with the impact of slower global economic growth. US economic performance in the period ahead will, however, be shaped by the United States' relations with its trading partners – in particular with China, on which the US recently imposed further trade restrictions. The optimism generated by US-Chinese discussions at the end of last year and start of this year did not result in progress, and on 10 May 2019 the US Administration increased tariffs from 10% to 25% on USD 200 billion worth of Chinese goods.⁴ According to the US, the tariff hike was a response to Chinese attempts to backtrack on commitments under draft US-China trade pact. China retaliated on 1 June 2019 by raising import tariffs of 5% or 10% on USD 60 billion worth of US goods to 10% or 25%. The trade dispute escalated further when the US Administration indicated its intention to impose a 25% tariff on the remaining Chinese imports, worth approximately USD

³ The US federal government shutdown lasted from 22 December 2018 to 25 January 2019.

⁴ The US Administration was originally planning to raise tariffs from 1 January. This deadline was postponed initially by three months, following a temporary trade truce agreed between the two countries in December 2018, and then again in February, following progress in bilateral talks.

300 billion. As regards its plans for applying tariffs to other trading partners, the Administration announced on 17 May 2019 that it was postponing for 180 days a decision on whether to impose tariffs on imported cars and auto parts,⁵ so as to allow for more time for trade talks with the European Union and Japan. The European Commission made clear that any measures harmful to European exports would result in retaliatory measures. At the end of May the US said it planned to impose a 5% tariff on all imports from Mexico with the option of increasing it later. But after bilateral talks, in which Mexico agreed to stem the flow of illegal migrants into the United States, the Administration decided not to proceed with the measure.

Annual consumer price index (CPI) inflation in the United States moderated in the first quarter of 2019, continuing the downward trend seen in the second half of 2018. Looking ahead, the increase in import tariffs on Chinese goods may have an upward impact on CPI inflation, or, on the other hand, the impact of the tariff hike may be offset by depreciation of the Chinese current and the trimming of profit margins. Furthermore, core inflation may have a dampening effect on the headline rate, owing to slower unit labour cost growth.

At its meetings in January, March and April/May 2019, the US Federal Open Market Committee (FOMC) decided to leave the target range for the federal funds rate unchanged at 2.25% to 2.50%. In its post-meeting statement in May, the Committee noted the strength of the labour market, the solid rate of economic activity growth, the low level of inflation, and the low survey-based measures of longer-term inflation expectations.

⁵ In mid-February, after completing an investigation initiated in May 2018, the US Commerce Department sent the US President a report (not published) on whether imports of cars and auto parts constitute a national security threat. In May 2019 the President announced that he agreed with report's findings that such imports do constitute a national security threat.

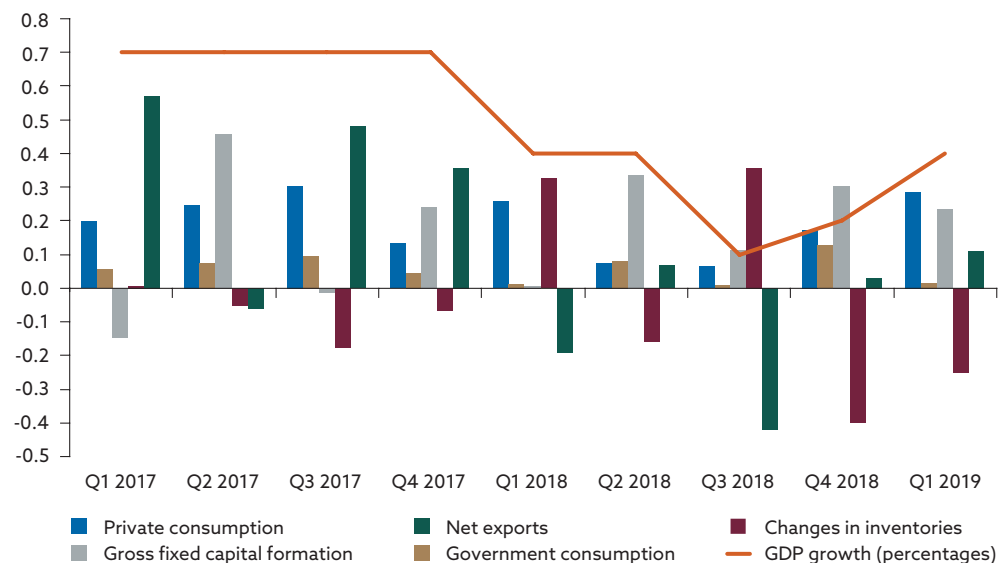
4 The euro area

Euro area GDP grew by 0.4%, quarter on quarter, in the first quarter of 2019, which represented a notable acceleration compared with the fourth quarter of the previous year (0.2%). Looking at the region's largest economies, Germany recorded the largest acceleration in GDP growth (from 0% in the fourth quarter to 0.4% in the first quarter), ahead of Spain (from 0.6% to 0.7%) and Italy, whose GDP growth increased to 0.1% after contracting by 0.1% in the previous period. In France, by contrast, GDP growth slowed (by 0.1 percentage point, to 0.3%), while in the Netherlands it remained unchanged (at 0.5%). In year-on-year terms, euro area GDP was the same in the first quarter of 2019 as in the previous quarter, at 1.2%.

The quarterly increase in economic activity growth was supported mainly by domestic demand, largely through stronger growth in private consumption. By contrast, government consumption growth decelerated. Investment demand growth remained relatively robust in the first quarter, albeit somewhat more moderate than in the previous quarter. It was driven mainly by stronger growth in construction investment, which benefited from good weather. There was also, however, higher growth in machinery and equipment investment and in transport investment. GDP growth was further boosted by net exports, as the impact of the quite large slowdown in export growth was more than offset by the drop in import growth. Exports may have partly benefited from stock-building by businesses in the UK ahead of the original Brexit date. There was downward pressure on economic growth from inventories, albeit more moderate than in the previous quarter.

Chart 2

Euro area GDP and its components (quarter-on-quarter percentage changes; percentage point contributions)

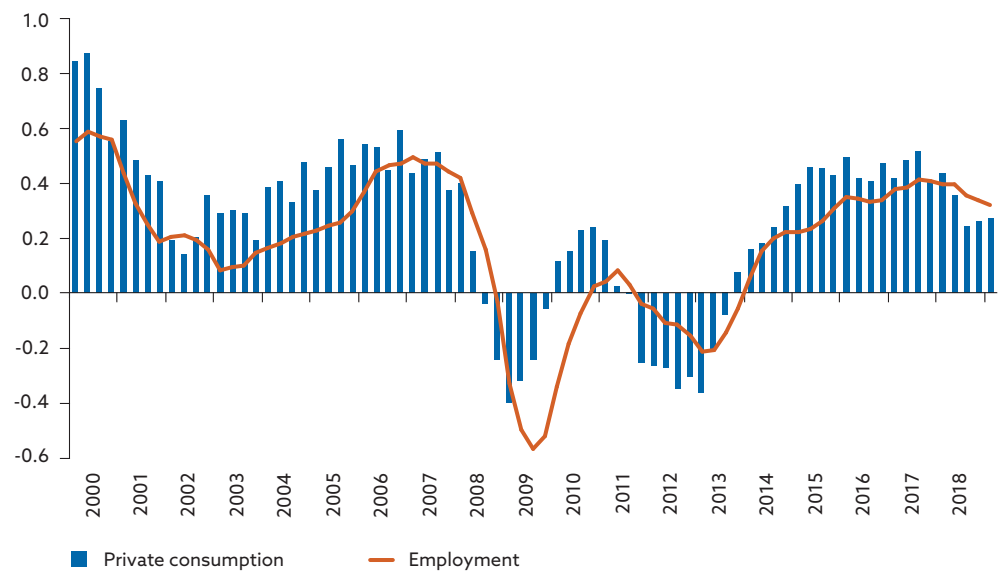


Sources: Macrobond and NBS calculations.

Private consumption growth recorded its strongest acceleration in four quarters, increasing from 0.3% in the fourth quarter to 0.5% in the first quarter. Consumer spending continued to be supported by the favourable labour market situation. Employment growth remained unchanged from the previous quarter (at 0.3%) and accompanied by relatively favourable wage developments. Despite the labour market buoyancy, however, consumers' expectations about the general economic situation deteriorated for a fourth successive quarter. This trend is gradually passing through to the saving ratio, which increased slightly in both the third and fourth quarters of 2018.⁶ A further decline in consumer sentiment and the economic outlook may therefore incentivise consumers to build up savings, thereby weakening consumer spending.

Chart 3

Private consumption and employment (quarter-on-quarter percentage changes; calculated from moving averages for four quarters)

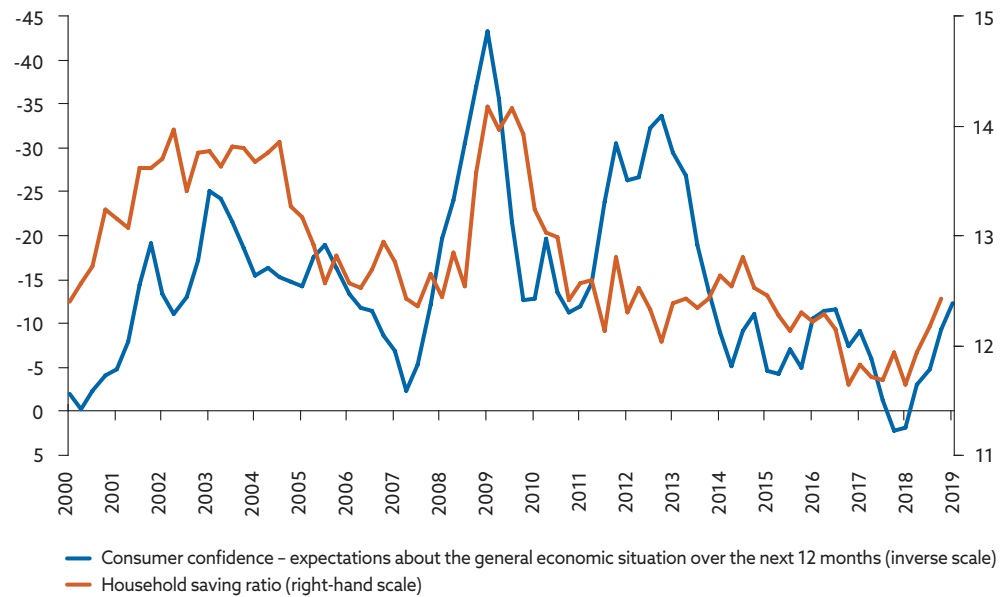


Source: Macrobond.

⁶ Saving ratio data for the first quarter of 2019 were not available by the cut-off date for this report.

Chart 4

The saving ratio and consumers' expectations about the general economic situation (percentages and percentage balances)

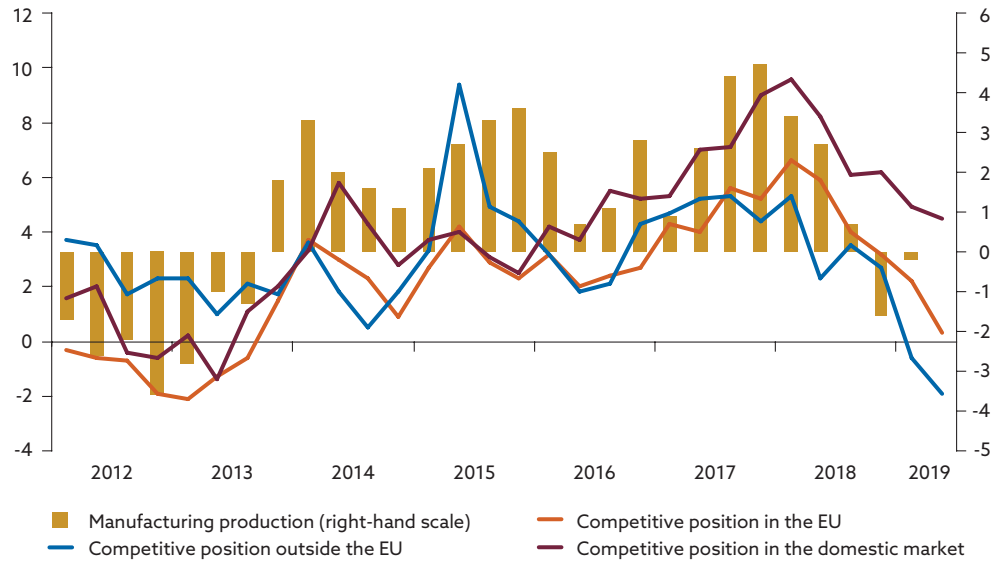


Source: Macrobond.

After falling in the last two quarters of 2018, euro area industrial production increased, quarter on quarter, by 0.9% in the first quarter of 2019. After surging in January, however, it remained flat in February and declined in March. Industrial production continued falling in April and, according to leading indicators, it is likely to remain subdued. As in the first quarter, industrial firms' assessments of their competitive position deteriorated in the second quarter of 2019. This decline stemmed mainly from assessments of competitiveness in EU and extra-EU markets and to a lesser extent in respect of domestic markets. At the same time, export expectations also continued to falter amid rising protectionism and cooling of the global economy.

Chart 5

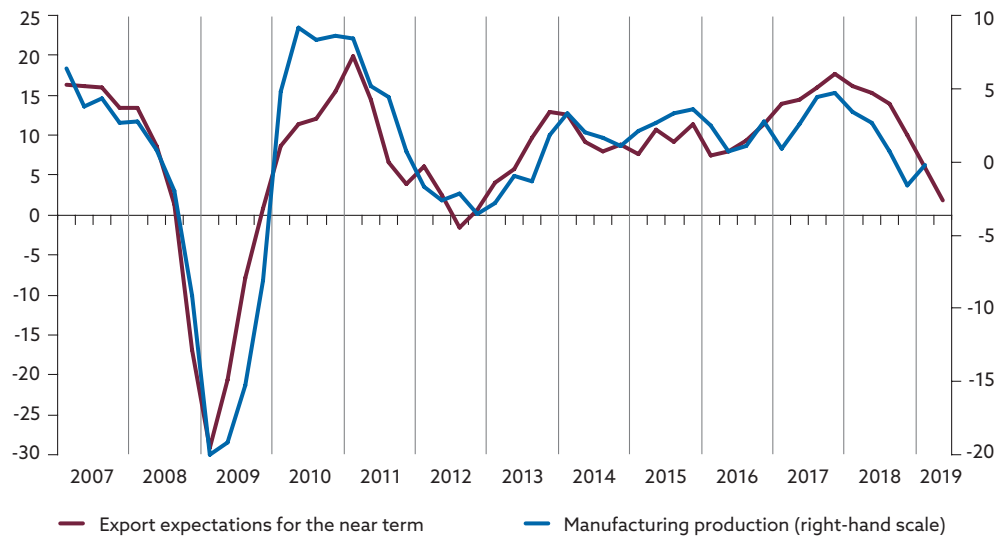
Industrial competitiveness and manufacturing production (percentage balances; annual percentage changes)



Sources: European Commission, Eurostat and NBS calculations.

Chart 6

Export expectations in industry and manufacturing production (percentage balances; annual percentage changes)



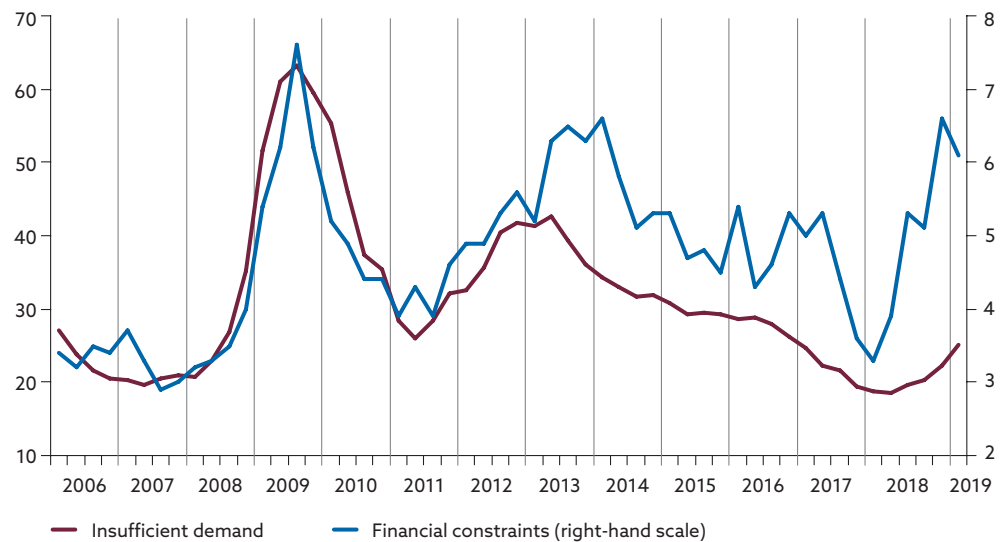
Sources: European Commission, Eurostat and NBS calculations.

Industrial firms' assessments of the factors limiting their production also imply a slowdown in economic activity growth. Survey results for the second quarter, as for the previous three quarters, showed an increase in the percentage of respondents reporting 'insufficient demand' as a factor limiting production. By contrast, after increasing significantly in the first quarter, the importance of 'financial constraints' fell slightly, with responses possibly swayed by the March decision of the ECB's Governing Council to

launch a new series of longer-term refinancing operations (TLTRO III).⁷ As for production factors – ‘shortage of material and/or equipment’ and ‘shortage of labour force’ – the share of respondents who see them as limiting production decreased again. Although the importance of these factors remains relatively elevated, its decrease implies an easing of labour market conditions as well as less demand for new investment.

Chart 7

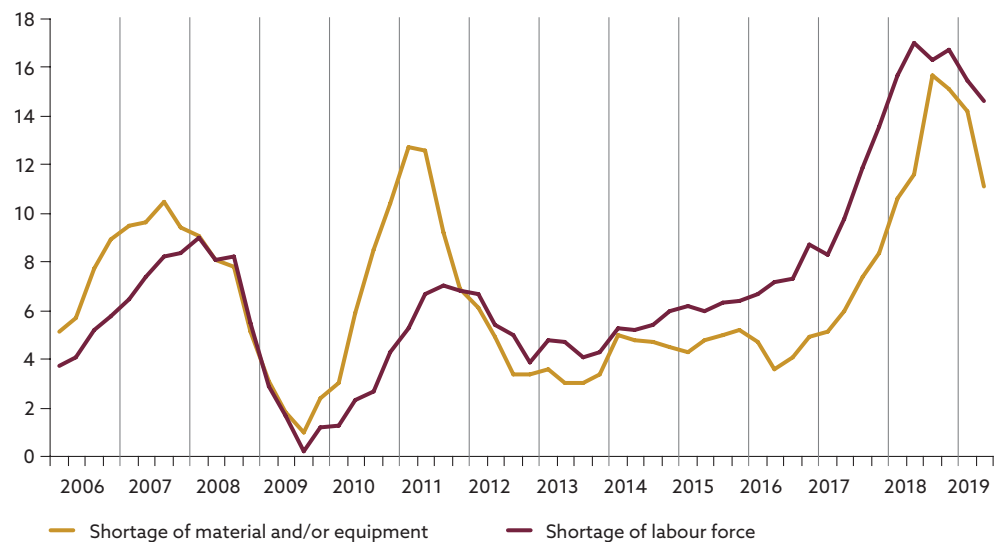
Factors limiting production in industry (percentages)



Source: Macrobond.

Chart 8

Factors limiting production in industry (percentages)



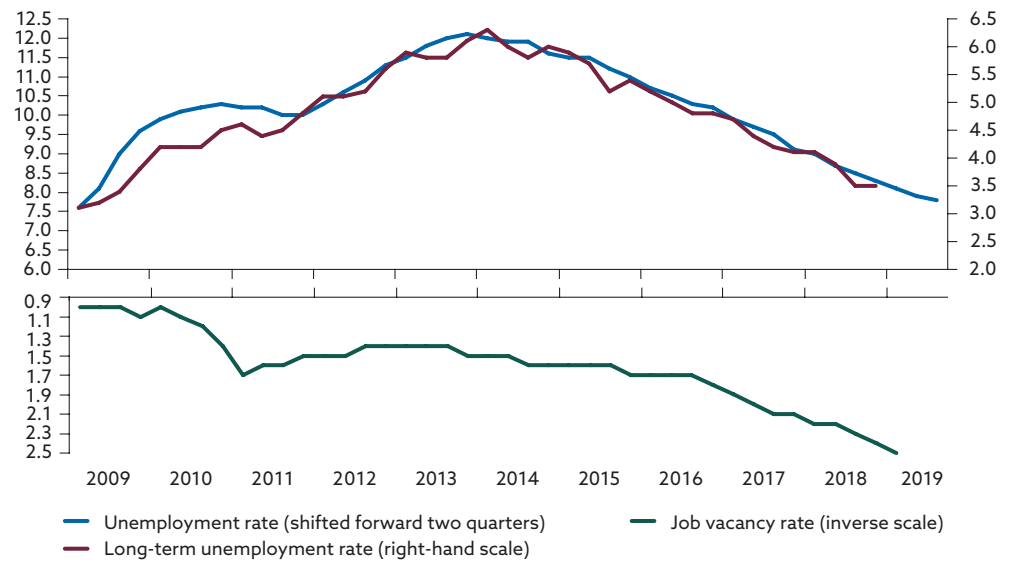
Source: Macrobond.

⁷ The survey did not reflect the impact of decisions taken at the ECB’s Governing Council meeting in June.

The unemployment rate continued its moderate downward trend in the first quarter, falling from 7.9% in December 2018 to 7.7% in March 2019. In April the rate edged down again, to 7.6%, just 0.3 percentage point above its pre-crisis low. Meanwhile, the job vacancy rate again increased moderately. Developments in unemployment, the job vacancy rate and employment point to continuing labour market buoyancy, despite weaker signals from leading indicators. There was a cross-sector deterioration in employment expectations in the first quarter and subsequent two months. This decline was most pronounced in the construction and industry sectors.

Chart 9

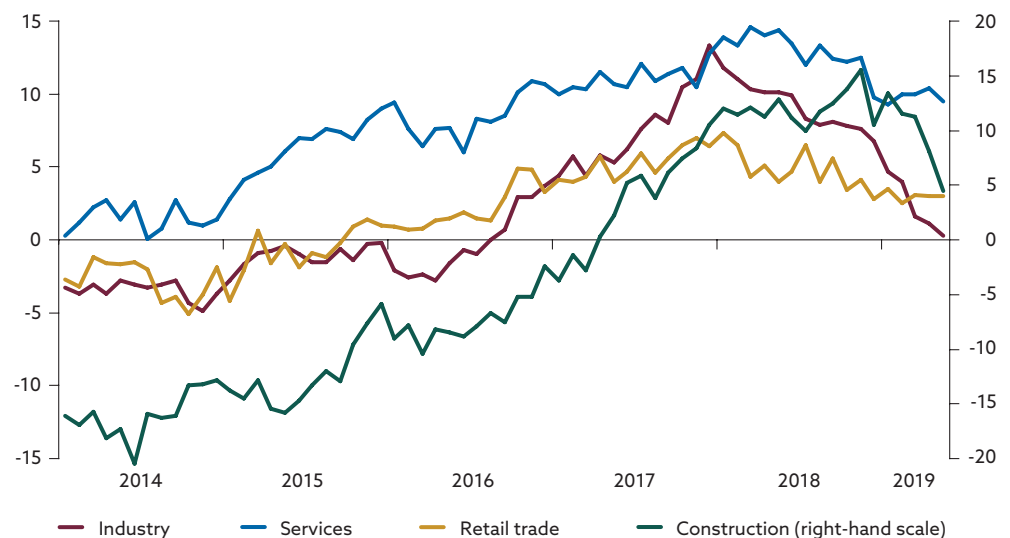
The unemployment rate, long-term unemployment rate, and job vacancy rate (percentages)



Source: Macrobond.

Chart 10

Employment expectations by sector (percentage balances)

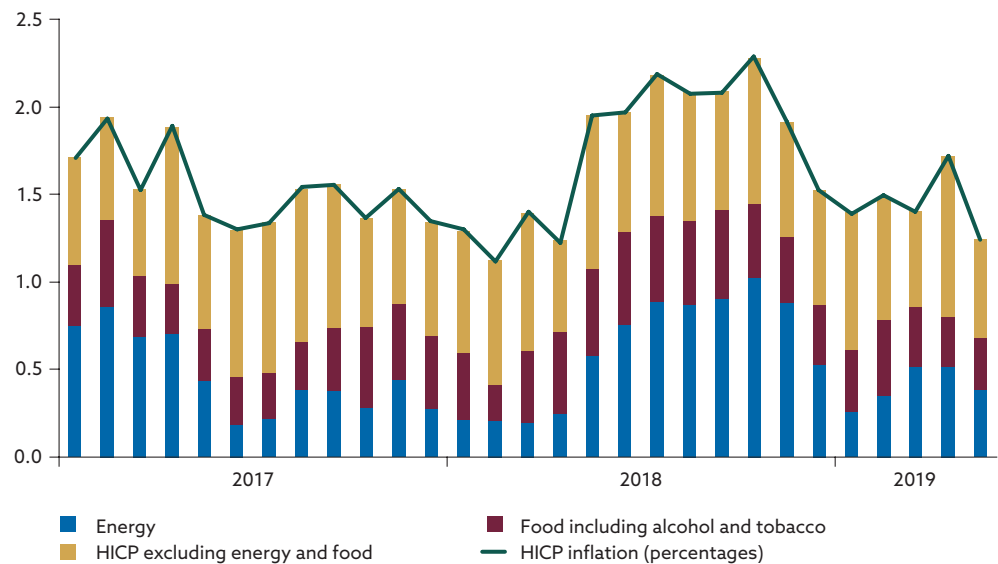


Source: Macrobond.

Euro area annual HICP inflation did not change significantly in the first quarter of 2019. The headline inflation rate was 1.4% in March, while in December 2018 it stood at 1.5%. There were, however, more pronounced changes in the breakdown of inflation, with the energy component gradually increasing and the services component decreasing, one impact offsetting the other. Non-energy industrial goods inflation also slowed moderately. Core inflation (HICP inflation excluding energy and food) was 0.3 percentage point lower in March (0.8%) than in December. Owing to the timing of the Easter holidays, which fell in April this year and in March last year, services inflation slowed in March and spiked in April, before decelerating again in May. This volatility was reflected in both headline inflation and core inflation, which accelerated in April, to 1.7% and 1.3% respectively, before moderating in May, to 1.2% and 0.8%. Another factor behind May's lower headline rate was a slowdown in energy inflation.

Chart 11

HICP inflation and selected components (annual percentage changes; percentage point contributions)

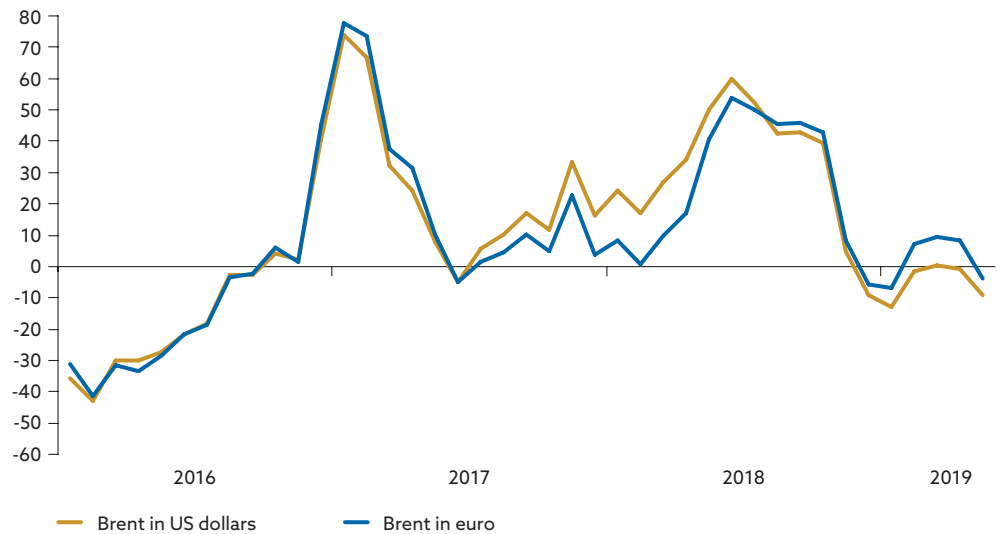


Source: Macrobond.

After falling in the last months of 2018, the euro oil price gradually rebounded in the first quarter of 2019. This trend had an upward impact on consumer energy price inflation, which after declining in January, accelerated in the next two months. In May, year-on-year oil prices started falling again and putting downward pressure on energy inflation, which again declined.

Chart 12

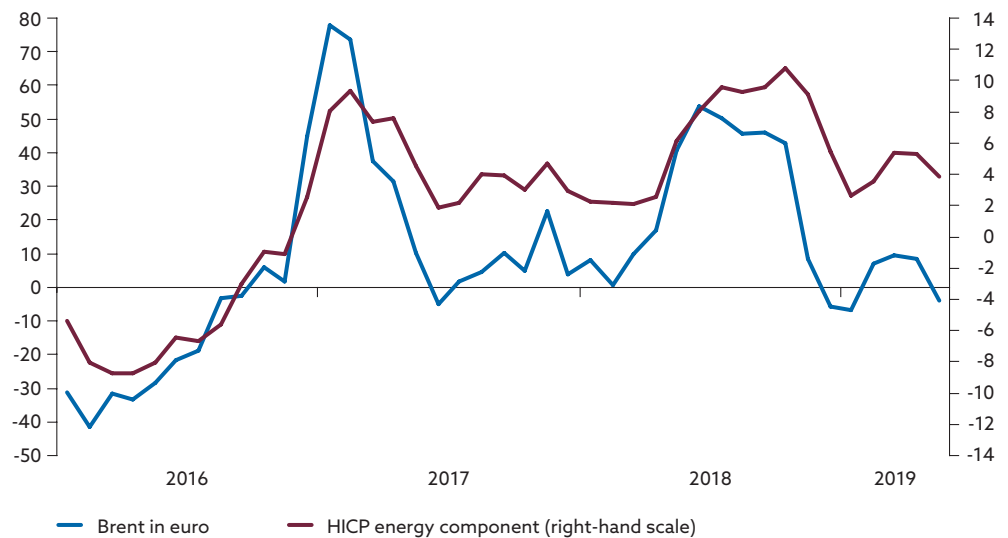
Oil prices in euro and US dollars (annual percentage changes)



Sources: Macrobond and NBS calculations.

Chart 13

Oil prices in euro and the HICP energy component (annual percentage changes)

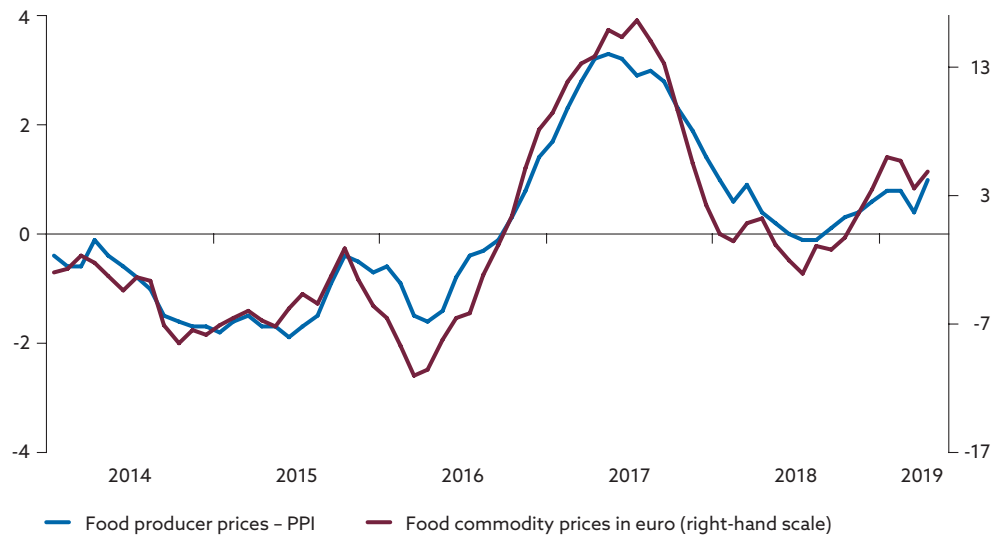


Sources: Macrobond and NBS calculations.

Cost pressures from food commodity prices have shown a slightly rising trend so far this year. The movements of both commodity prices and producer prices were affected by calendar effects related to the Easter holidays, which resulted in price growth decelerating in March and accelerating in April. Since September 2018, however, food producer prices have been on a slightly upward trend, reflecting movements in food commodity prices. Nevertheless, this increasing price pressure from food producers has not so far had a significant impact on processed food consumer prices, whose inflation rate has remained broadly unchanged over the same period.

Chart 14

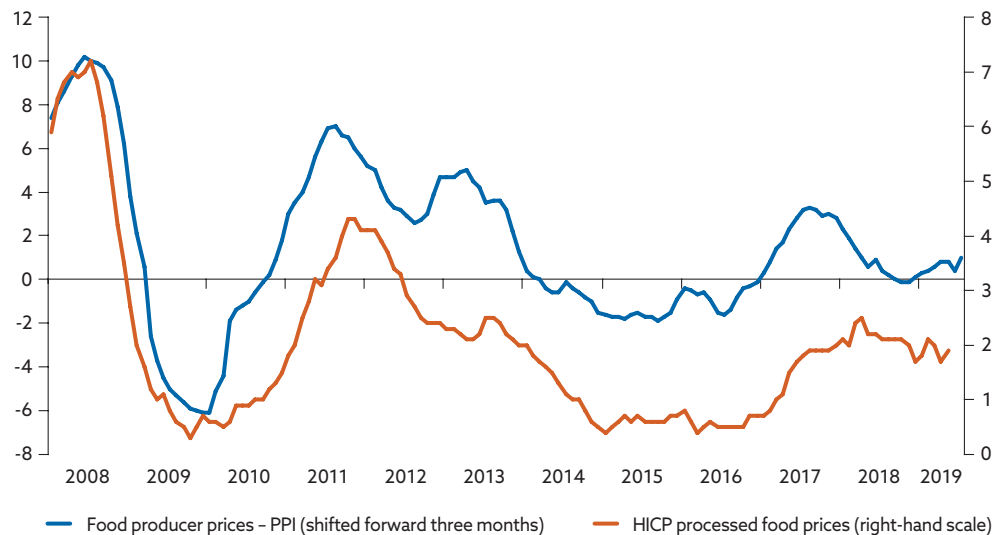
Food commodity and producer prices (annual percentage changes)



Source: Macrobond.

Chart 15

Food producer prices and processed food prices (annual percentage changes)



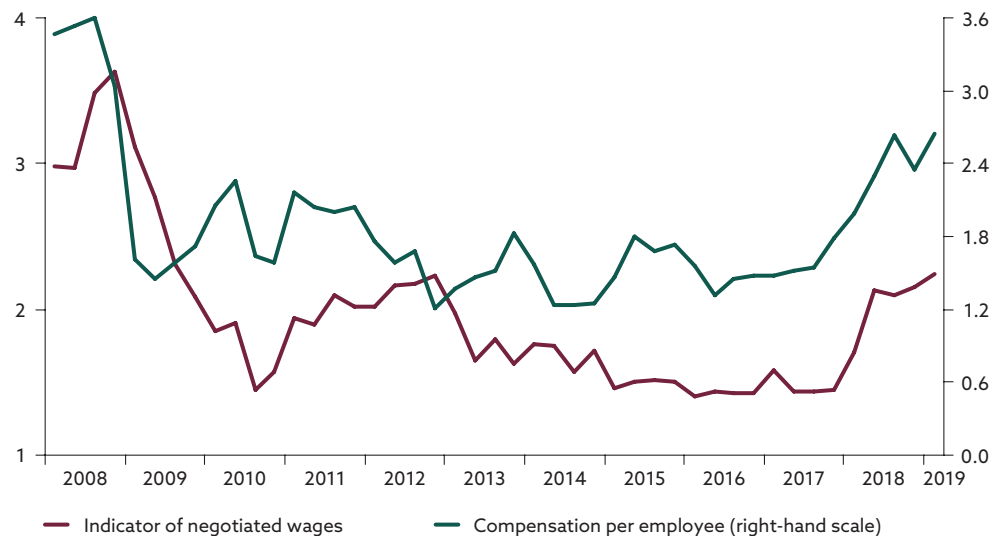
Source: Macrobond.

Core inflation was relatively subdued during the first quarter of 2019, and its rate in March (0.8%) was similar to its rate in December 2018 (0.1 percentage point lower). After increasing moderately in January, core inflation declined in the next months, especially so in March owing to the timing of Easter. The period from March to May was marked by higher volatility in services inflation, in particular services related to recreation and transport. After increasing to 1.3% in April, core inflation corrected in May, back to its March level of 0.8%. Following the fading of the calendar effects, core inflation is expected to increase in the subsequent period. Wage growth remained relatively strong in the first quarter of 2019, though without yet

passing through to headline inflation. At the same time, the downward revisions of GDP growth outlooks may indicate constraints on future wage growth and an additional factor limiting its pass-through to prices. The nominal effective exchange rate (NEER) depreciated moderately, year on year, in the first quarter of 2019. This trend was supported by import prices from late 2018, when their annual rate of change shifted from negative to positive. April and May saw an appreciable acceleration of import prices, which supported a slight increase in non-energy industrial goods inflation.

Chart 16

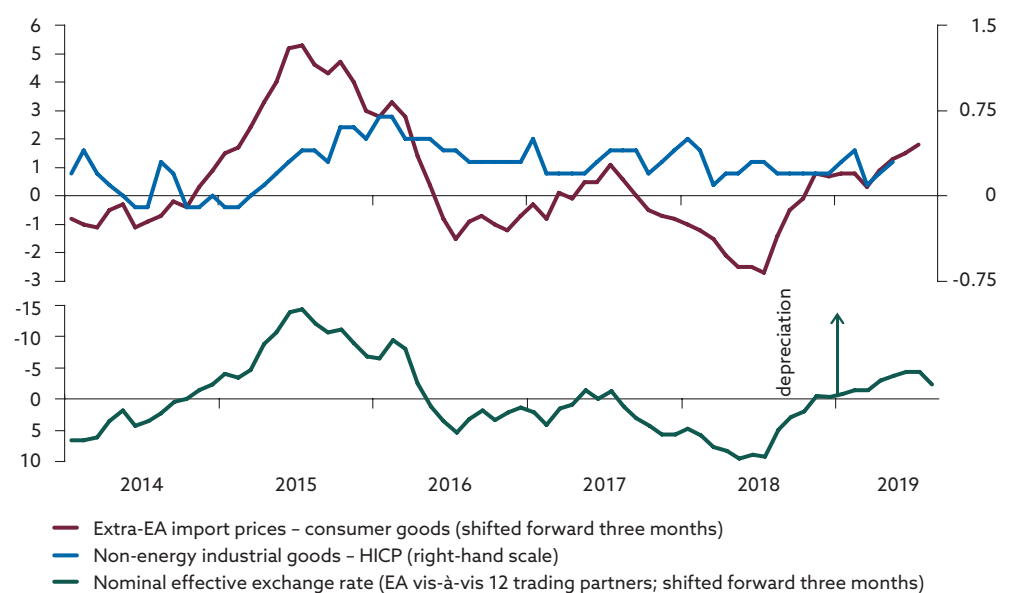
Wage developments (annual percentage changes)



Sources: Macrobond and NBS calculations.

Chart 17

Non-energy industrial goods prices and the nominal exchange rate (annual percentage changes)

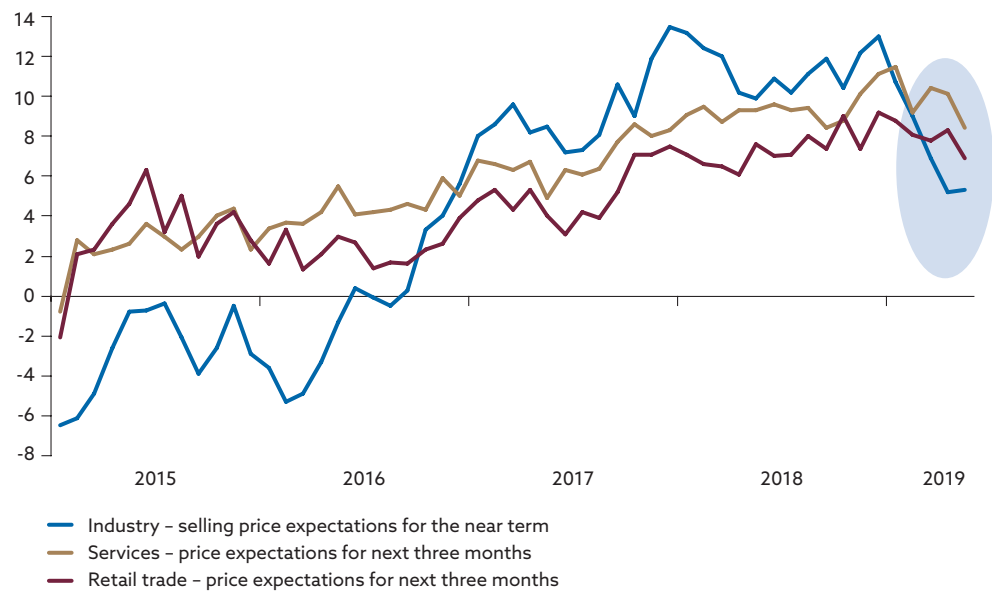


Source: Macrobond.

Rising uncertainty related to the escalation of protectionism and global economic slowdown has had a downward impact on price expectations. In an environment of strong competition and subdued economic outlooks, selling price expectations have been falling this year, most markedly in industry but also in the services and retail trade sectors. Meanwhile, for the second successive quarter, the ECB Survey of Professional Forecasters (for the second quarter of 2019) showed a downward revision of inflation expectations, both for this year and 2020.

Chart 18

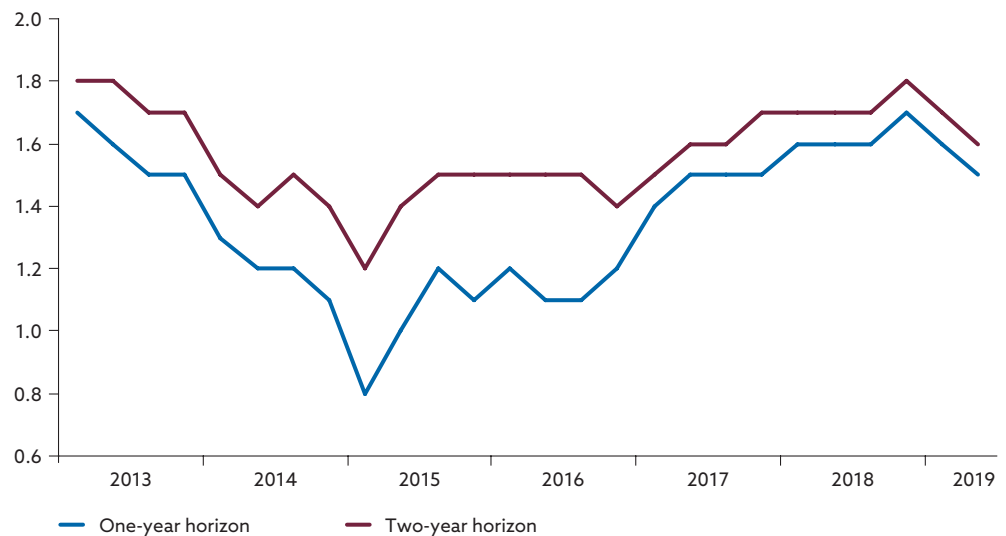
Price expectations in industry, services and retail trade (percentage balances)



Source: Macrobond.

Chart 19

Expectations for HICP inflation according to the ECB Survey of Professional Forecasters (percentages)



Source: Macrobond.

At its monetary policy meetings between January and June 2019, the ECB's Governing Council decided to leave the interest rates on the main refinancing operations, the marginal lending facility and the deposit facility unchanged at 0.00%, 0.25% and -0.40% respectively. The Governing Council expects that rates will remain at their present levels at least through the first half of 2020, and in any case for as long as necessary to ensure the continued sustained convergence of inflation to levels that are below, but close to, 2% over the medium term.

In line with its enhanced forward guidance on reinvestment, set out in December 2018, the Governing Council stated after each of the above meetings that it intended to continue reinvesting, in full, the principal payments from maturing securities purchased under the asset purchase programme (APP) for an extended period of time past the date when it starts raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation. In addition, the Governing Council said the Eurosystem would continue conducting lending operations as fixed rate tender procedures with full allotment for as long as necessary, and at least until the end of the reserve maintenance period starting in March 2021. In March 2019 the Governing Council decided to launch a new series of quarterly targeted longer-term refinancing operations (TLTRO III), starting in September 2019 and ending in March 2021, each with a maturity of two years. Under TLTRO III, counterparties will be entitled to borrow up to 30% of the stock of eligible loans as at 28 February 2019 at a rate indexed to the interest rate on the main refinancing operations (MROs) over the life of each operation.

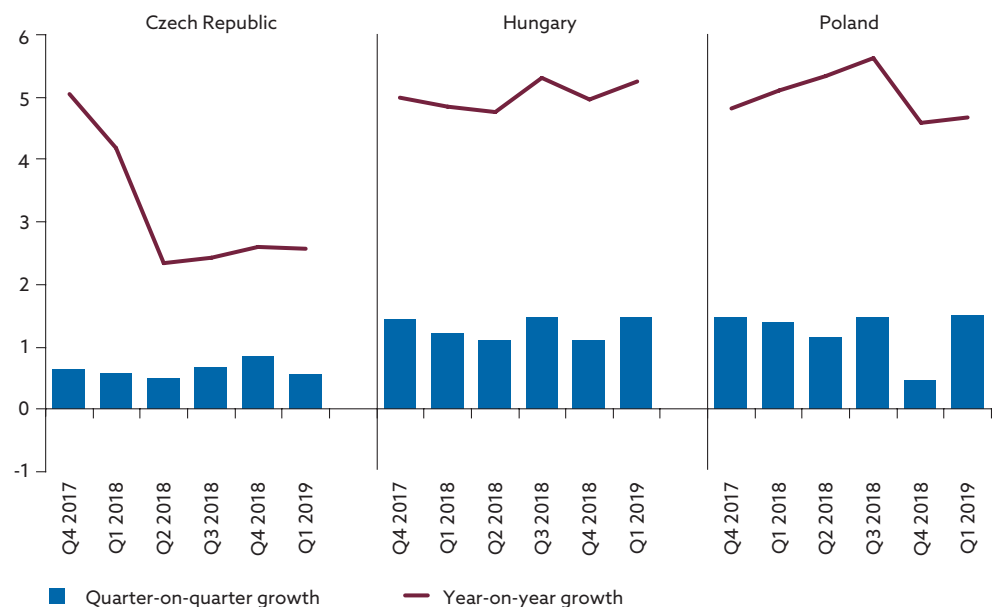
At its June meeting, the Governing Council adopted a decision on the modalities of TLTRO-III. The interest rate for each operation will be set at a level of 10 basis points above the average rate applied to the Eurosystem's MROs over the life of the respective TLTRO. For counterparties whose eligible net lending between the end of March 2019 and the end of March 2021 exceeds their benchmark net lending, the rate applied to TLTRO III operations will be lower, and can be as low as the average interest rate on the deposit facility prevailing over the life of the respective operation plus 10 basis. Counterparties will receive the maximum rate reduction if they exceed their benchmark stock of eligible loans by 2.5% as at 31 March 2021. Below this limit, the size of the decrease in the interest rate will be graduated linearly depending on the percentage by which a counterparty exceeds its benchmark stock of eligible loans. For counterparties that exhibited positive eligible net lending in the 12-month period to 31 March 2019, the benchmark net lending is set at zero. For counterparties that exhibited

negative eligible net lending in the 12-month period to 31 March 2019, the benchmark net lending is equal to the eligible net lending in that period. The interest rate applied to TLTRO III operations will be communicated to participants in September 2021.

5 The Czech Republic, Hungary and Poland

In Hungary and Poland, annual GDP growth was higher in the first quarter of 2019 than in the fourth quarter of 2018, while in the Czech Republic it remained unchanged, at 2.6%. Hungary's growth accelerated by 0.2 percentage point, to 5.2%, and Poland's by 0.1 percentage point, to 4.7%.

Chart 20
GDP (percentage shares)



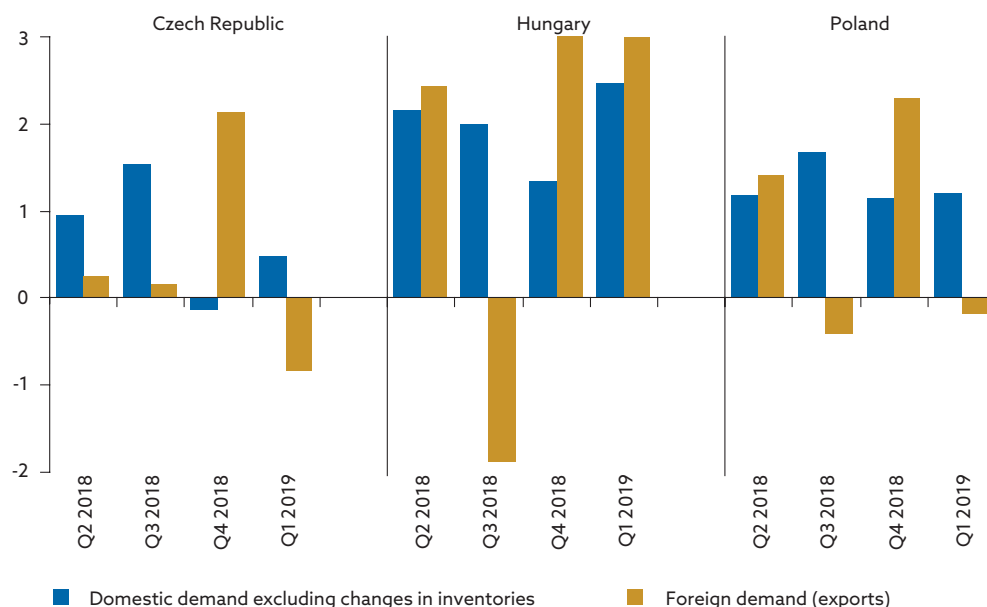
Source: Eurostat.

In quarter-on-quarter terms, too, GDP growth increased in Hungary (by 0.4 percentage point, to 1.5%) and Poland (by 0.6 percentage point, to 1.5%). By contrast, Czech economic growth slowed by 0.2 percentage point, to 0.6%. The decrease in Czech GDP growth stemmed mainly from net exports, which in the previous quarter had made a positive contribution. Investment demand also had a dampening effect on growth. The positive contributions to the Czech Republic's quarter-on-quarter economic growth came mainly from private consumption and to a lesser extent from public consumption and changes in inventories. In Hungary, the pick-up in economic growth was largely attributable to investment demand. There was also a smaller positive contribution from government consumption expenditure, whose impact in the previous quarter had been negative. The positive contribution of net exports moderated, as export growth slowed significantly and import growth accelerated. The impact of private consumption was also less positive. Changes in inventories were a notable

drag on growth, more so than in the previous quarter. In Poland, firming investment demand was the main factor behind the increase in GDP growth. Both public and private consumption also had a positive impact. The contribution of net exports, by contrast, was strongly negative, owing to a decline in exports. Changes in inventories had a negative impact, too.

Chart 21

Contributions to quarterly GDP growth (percentage points)

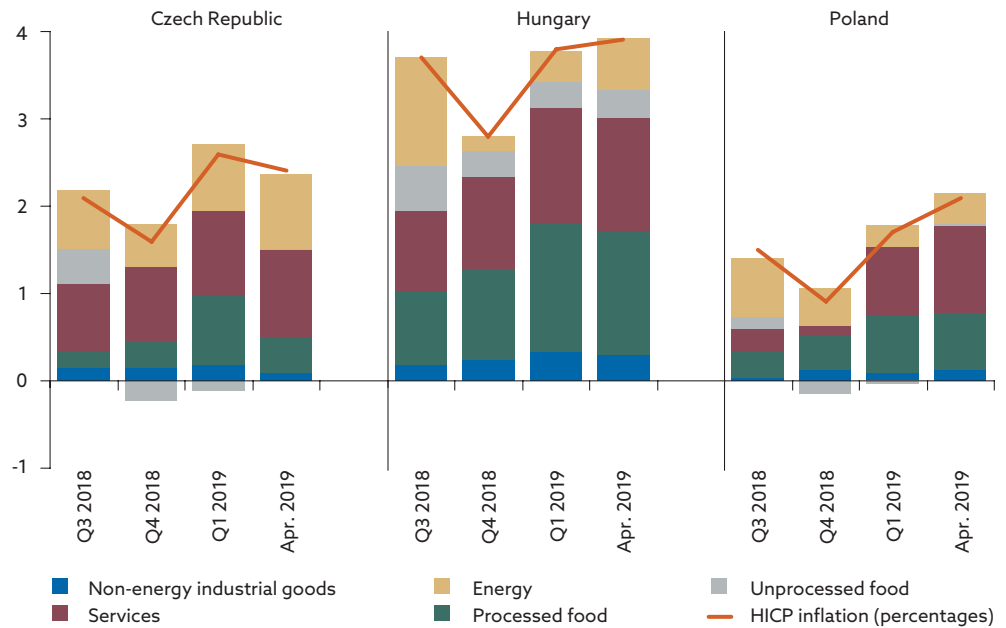


Sources: Eurostat and NBS calculations.

In all three countries, annual consumer price inflation was higher in March 2019 than in December 2018, accelerating in the Czech Republic by 1.0 percentage point, to 2.6%, in Hungary by 1.0 percentage point, to 3.8%, and in Poland by 0.8 percentage point, to 1.7%. In the Czech Republic, the rise in headline inflation was based mainly on increases in prices of processed food, energy, and services. At the same time, unprocessed food inflation moderated. The impact of the non-energy industrial goods component was the same in March as in December. In Hungary, all components supported the increase in headline inflation, and the largest contribution came from processed food inflation. In Poland, consumer price inflation was pushed up mainly by a sharp acceleration in services inflation and to a lesser extent by price movements of unprocessed food and processed food. The energy component's impact was less positive in March 2019 than in December 2018.

Chart 22

HICP inflation and its components (annual percentages; percentage point contributions)

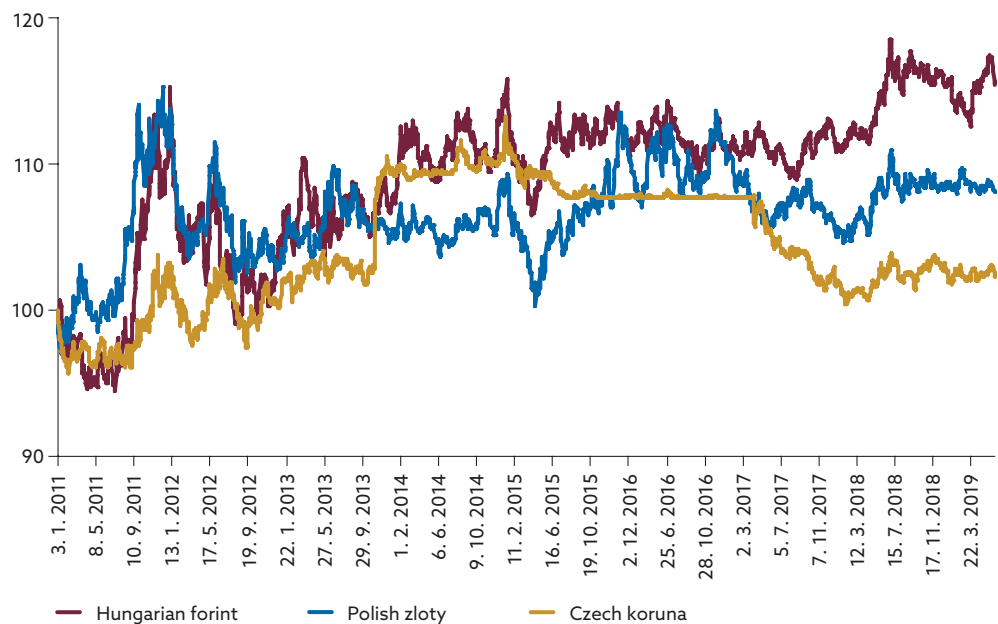


Sources: Eurostat and NBS calculations.

Comparing their exchange rates against the euro at the end of the first quarter of 2019 and at the end of the previous quarter, none of three countries' currencies showed any significant change: the Czech koruna was 0.30% weaker, while the Hungarian forint and Polish zloty were stronger, by 0.02% and 0.02% respectively.

Chart 23

Exchange rate indices of national currencies vis-à-vis the euro (index: 3 January 2011 = 100)



Sources: Eurostat and NBS calculations.

Note: A fall in value denotes appreciation.

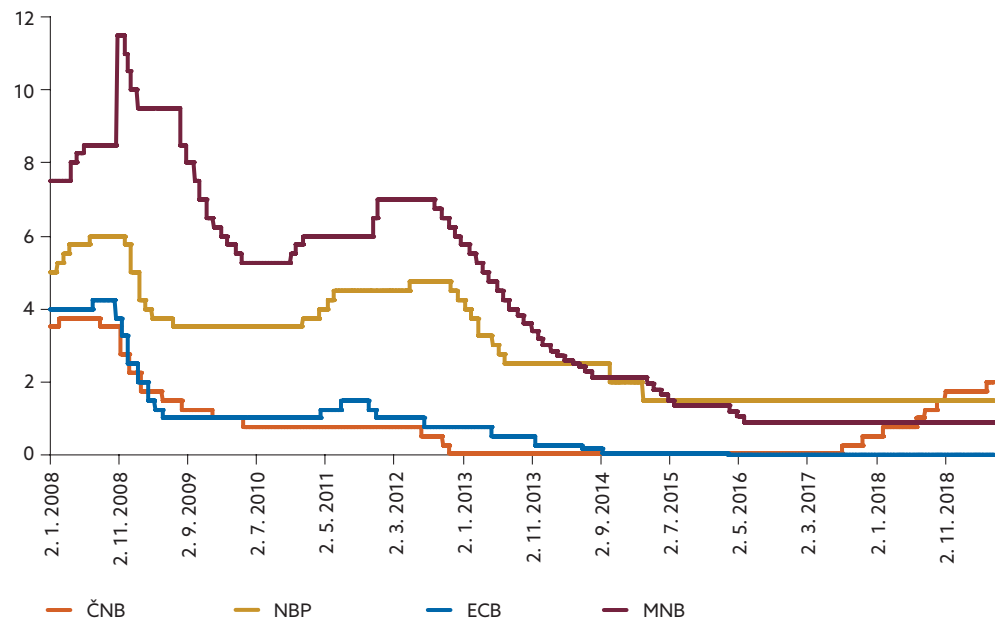
During the first quarter, the koruna's exchange rate oscillated around 25.7 per euro. The forint appreciated moderately for most of the period, before depreciating towards the end. As for the zloty, it weakened in February, but subsequently strengthened back to the level at which it began the year. In general, the exchange rates were affected by negative investor sentiment in financial markets, arising after international institutions revised down their outlooks for global economic growth. This was also related to the decisions of major central banks to pause monetary policy tightening. Sentiment was further dented by the risk of trade war escalation and by the postponement of the Brexit deadline until autumn 2019. Local factors also had an effect on the currencies under review. On the one hand, the very negative economic data from Germany in the first quarter, resulted in depreciation pressure on the forint and koruna, owing to the high economic openness of the Czech Republic and Hungary towards Germany (especially through car exports). On the other hand, favourable trends in the domestic economies (strong domestic demand driven mainly by consumption as well as by investment) may have put appreciation pressure on the currencies.

The Czech central bank, Česká národní banka (ČNB), left its monetary policy rates unchanged in the first quarter of 2019 on the grounds that the risks to the inflation forecast at the monetary policy horizon are broadly balanced and that broad interest rate stability is consistent with such forecast. The main upside risk to the inflation outlook remains lower than projected appreciation of the Czech koruna's exchange rate. The principal ongoing uncertainties concern the risk of a disorderly Brexit and increasing protectionism in world trade. In May 2019, after discussing the central bank's latest macroeconomic forecast and the risks surrounding it, the ČNB Bank Board raised the base interest rate by 25 basis points (to 2.00%). In Hungary, the Monetary Council of the Magyar Nemzeti Bank (MNB) decided at its meeting on 26 March 2019 to raise its overnight deposit rate by ten basis points, -0.05%, while leaving the base rate, the overnight collateralised lending rate and the one-week collateralised lending rate unchanged at 0.9%. In explaining the decision, the MNB said it had met its inflation target (with CPI inflation at around 3% since mid-2018 and core inflation rising to 3% at the start of the year) and that the deposit rate increase was necessary to maintain price stability. In addition, the MNB reduced the average amount of liquidity to be crowded-out for the second quarter of 2019 by HUF 100 billion, to at least HUF 300-500 billion, and will take this into account in setting the stock of swap instruments providing forint liquidity. Furthermore, to improve the effectiveness of monetary policy transmission, the Monetary Council decided in March to launch a corporate bond purchasing programme – the Bond Funding for Growth Scheme (BGS) – on 1 July 2019, with the total amount of purchases set at

HUF 300 billion. This new non-standard monetary policy instrument is designed to promote the diversification of funding to the domestic corporate sector. The BGS will complement the Funding for Growth Scheme Fix launched at the beginning of 2019. In Poland, Narodowy Bank Polski (NBP) left its monetary policy rates unchanged in the first quarter of 2019 (the reference rate has been at 1.5% since 5 March 2015). The central bank reiterated its view, based on incoming data and forecasts, that the current level of interest rates was conducive to keeping the Polish economy on a sustainable growth path and maintaining macroeconomic stability.

Chart 24

Key interest rates of the Czech, Polish and Hungarian central banks and the ECB (percentages)



Sources: ČNB, NBP, MNB and ECB.

Summary of GDP growth projections of selected institutions

Table 1 Global economy

	Release	2018		2019		2020		2021	
IMF	April 2019	3.6	(-0.1)	3.3	(-0.2)	3.6	(=)	-	-
OECD	May 2019	3.5	(-0.1)	3.2	(-0.1)	3.4	(=)	-	-
EC ¹⁾	May 2019	3.9	(-0.1)	3.6	(-0.2)	3.8	(=)	-	-
ECB ²⁾	June 2019	3.8	(0.1)	3.3	(-0.2)	3.6	(=)	3.6	(=)

Table 2 United States

	Release	2018		2019		2020		2021	
IMF	April 2019	2.9	(=)	2.3	(-0.2)	1.9	(0.1)	-	-
OECD	May 2019	2.9	(=)	2.8	(0.2)	2.3	(0.1)	-	-
EC	May 2019	2.9	(=)	2.4	(-0.2)	1.9	(=)	-	-
Federal Reserve	March 2019	2.9	(=)	2.05	(-0.35)	1.9	(=)	1.85	(0.1)

Table 3 Euro area

	Release	2018		2019		2020		2021	
IMF	April 2019	1.8	(=)	1.3	(-0.3)	1.5	(-0.2)	-	-
OECD	May 2019	1.8	(=)	1.2	(0.2)	1.4	(0.2)	-	-
EC	May 2019	1.9	(=)	1.2	(-0.1)	1.5	(-0.1)	-	-
ECB	June 2019	1.8	(-0.1)	1.2	(0.1)	1.4	(-0.2)	1.4	(-0.1)

Table 4 Czech Republic

	Release	2018		2019		2020		2021	
IMF	April 2019	2.9	(-0.2)	2.9	(-0.1)	2.7	-	-	-
OECD	May 2019	2.9	(-0.1)	2.6	(-0.1)	2.5	(-0.1)	-	-
EC	May 2019	2.9	(=)	2.6	(-0.3)	2.4	(-0.3)	-	-
ČNB	May 2019	2.9	(0.1)	2.5	(-0.4)	2.8	(-0.2)	-	-

Table 5 Hungary

	Release	2018		2019		2020		2021	
IMF	April 2019	4.9	(0.9)	3.6	(0.3)	2.7	-	-	-
OECD	May 2019	5.0	(0.4)	3.9	(=)	3.0	(-0.3)	-	-
EC	May 2019	4.9	(0.1)	3.7	(0.3)	2.8	(0.2)	-	-
MNB	March 2019	4.9	(0.2)	3.8	(0.3)	3.2	(0.2)	3.0	-

Table 6 Poland

	Release	2018		2019		2020		2021	
IMF	April 2019	5.1	(0.7)	3.8	(0.3)	3.1	-	-	-
OECD	May 2019	5.1	(-0.1)	4.2	(0.2)	3.5	(0.2)	-	-
EC	May 2019	5.1	(=)	4.2	(0.7)	3.6	(0.4)	-	-
NBP	March 2019	5.1	(0.3)	4.0	(0.4)	3.7	(0.3)	3.5	-

1) Global economic growth excluding the EU.

2) Global economic growth excluding the euro area.

Note: Data in brackets denote the percentage point change from the previous projection.